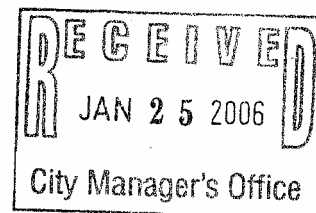




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JAN 20 2006

Ms. Amy Chang  
City Manager  
City of Sunnyvale  
P.O. Box 3707  
Sunnyvale, CA 94088-3707

Subject: Results of Program Monitoring  
Community Development Block Grant Program:  
B03-MC-06-0023 and B04-MC-06-0023  
HOME Investment Partnerships Program:  
M02-MC-06-0222 through M04-MC-06-0222

Dear Ms. Chang:

The purpose of this letter is to report the results of our program monitoring review of the City of Sunnyvale's Community Development Block Grant (CDBG) and HOME Investment Partnerships Programs, conducted August 31, September 20 & 21, 2005, by Rafael Cedillos, Senior Community Planning and Development Representative.

The objective of the monitoring review was to determine compliance with applicable CDBG and HOME statutory requirements and program regulations, as well as provide any necessary technical assistance to the City to improve program delivery, effectiveness and administrative efficiency.

The administration and operation of both programs by the Community Development Department was determined to be highly efficient and accomplishments were consistent with respective Annual Action Plans and reporting submissions to HUD-CPD, as well as the City's five-year Consolidated Plan.

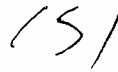
We reported one finding regarding an ineligible activity funded under the CDBG Program and one concern pertaining to revised policies and procedures for the HOME Programs. We shared the review results with Mr. Robert Paternoster, Community Development Director, and Ms. Annabel Yurutucu, Housing Preservation Officer, at our exit conference held on September 28, 2005.

Our monitoring report covering the CDBG and HOME programs is enclosed. We apologize for the delay in issuing the monitoring report. However, additional time was necessary for our office to work with City staff and consult with our HUD-CPD staff in Washington, D.C., to explore the most feasible way to resolve the CDBG finding, based on the most current CDBG policy.

Within 30 days from the date of this letter, the City must respond to required actions described in the report in order to resolve the sole finding. Although it is optional on the City's part, we would appreciate being informed regarding any plans that the City intends to implement with respect to the noted concern and recommended actions.

We wish to thank the Community Development Department staff for the assistance and cooperation provided. If you have any questions, please contact Rafael Cedillos at (415) 436-8493.

Very sincerely yours,



Maria Cremer  
Program Manager  
Community Planning  
and Development Division

Enclosure

cc: Robert Paternoster  
Director, Community Development Department

Annabel Yurutucu  
Housing Officer/ CDD

✓ Katrina Ardina  
Housing Finance Specialist/ CDD

**Addendum**

**CDBG Program**

**Compliance with National Objectives**

Section 101 (c) of the authorizing statute sets forth the primary objective of the CDBG program as the development of viable communities by the provision of decent housing and a suitable living environment and expanding economic opportunities, principally for persons of low and moderate income. The statute further states that this is to be achieved in the CDBG program by ensuring that each funded activity meets one of the three national objectives: activities benefiting low and moderate-income persons; preventing or eliminating slums or blight; or meeting urgent needs. The statute also states that each grantee must ensure that at least 70% of its expenditures over a one, two, or three year period must be used for activities qualifying under the first national objective, benefiting low-and moderate-income persons.

The activities in the City's CDBG program were reviewed and found to be in compliance with low and moderate-income benefit national objectives, as well as program requirements applicable at the time the City's 2003 and 2004 Annual Action Plans were prepared and submitted. The following projects reviewed were determined to have met the national objective of benefiting low and moderate-income persons on a limited clientele, slum and blight area and housing basis, respectively: EHC/Our House Homeless Youth Shelter, a public facility and the three public services noted above, the Neighborhood Enhancement Project, public improvement activity only and the Homestead Park multi-unit rental housing plus single-family, owner-occupied rehabilitation projects.

**Eligibility**

Under the category of Public Services found at 24 CFR 570.201 (e) of the CDBG regulations, Entitlement funds may be used to provide public services (including labor, supplies, materials, and other costs), provided that the following criteria is met:

- 1) The public service must be either a new service; or a quantifiable increase in the level of a service above that which has been provided by or on behalf of the unit of general local government through funds raised by such unit, or received by such unit from the State in which it is located during the 12 months prior to the submission of the grantee's applicable Action Plan.
- 2) The amount of CDBG funds obligated within a program year to support public service activities under this category may not exceed 15% of the total grant awarded to a grantee for that year plus 15% of the total program income it received in the preceding program year.

Based on our review of the City's files, other programmatic records and reporting information, we determined that public service activities selected for our review, i.e., First United Methodist Church, Catholic Charities and Emergency Housing Consortium, were eligible under the CDBG program. Documentation supporting this determination was found in each file we examined. In addition, the City complied with the 15% public service cap for the 2003 and 2004 Program Years.

In the CDBG Program, site improvements that are made to property that is in public ownership, with certain exceptions, are considered to be Public Improvements eligible under 24 CFR 570.201( c ) of the regulations. Entitlement funds may be used for such public improvements as streets, sidewalks, curbs and gutters, parks, playgrounds, water and sewer lines, flood and drainage improvements, parking lots, utility lines and certain aesthetic amenities on public property, e.g., trees. Additionally, limited improvements to a deteriorating area as a prelude to permanent improvements may be carried out on an Interim Basis under 24 CFR 570.201(f), and may include the repair of streets, sidewalks and publicly-owned utilities, special garbage and debris removal and neighborhood cleanup campaigns (but not regular curbside collection of garbage). Improvements to private properties under this subpart is permitted, but only to alleviate an emergency condition.

The rehabilitation of private, residential properties which are occupied by low and moderate income owner-occupants is eligible under 24 CFR 570.202. The costs of installation or replacement of landscape materials, sidewalks and driveways when incidental to other rehabilitation of the property is also permitted. The income eligibility of beneficiaries may be waived only under certain exceptions, for example, when CDBG funded rehabilitation activities are part of a grantee's overall concerted effort to eliminate deteriorating conditions in a particular area or neighborhood which meets the criteria for applying the Slums and Blight on an Area Basis national objective.

**Finding No. 1: The landscaping of private front yards, as part of the Lakewood Village Neighborhood Enhancement Project is not an eligible CDBG public improvement or housing rehabilitation activity**

The Lakewood Village Neighborhood Enhancement Project is a viable effort, which has proven successful in deterring the decline of this neighborhood and the City's goals to improve the area are being achieved. Unfortunately, certain costs paid with CDBG funds have been determined not eligible by HUD, namely landscaping of private front yards. Following is a background summary of the project, the basis for HUD's determination and the required corrective action which the City employed to resolve this finding.

**Background**

- With the participation of local residents, the City of Sunnyvale, CA created a "pilot program" designating Lakewood Village as a neighborhood enhancement area.

Overall, 53 of 95 properties were improved externally by correcting code violations, which included illegal garage conversions, roof extensions and/or additions, junk/debris, abandoned vehicles, dilapidated/broken fences and overgrown vegetation.

- Several properties occupied by low and moderate-income owner-occupants received housing rehabilitation loans through the City's CDBG Rehabilitation Revolving Loan Fund. Fourteen owners painted their properties with free paint, which was donated by local painting contractors to the City.
- Lakewood Village met the State definition of a slum and blight area under State Redevelopment policy and the properties in the Lakewood Village area were found to have a higher concentration of exterior code violations, i.e., approx. 40%, as compared to any other neighborhood and 8% city-wide.
- The City of Sunnyvale has utilized approximately \$150,000 in CDBG funds over a two-year period (FYs 2003-04 and 2004-05), as part of a broader effort to improve physical deterioration conditions in the Lakewood Village neighborhood enhancement area.
- Essentially, 25% of CDBG funds has been used to repair public improvements, specifically sidewalks and 75% has been used to provide small grants to 25 owner-occupants to correct various site-specific code violations (such as noted above), with the added benefit of improving the appearance of each property and in turn the neighborhood. The neighborhood enhancement project has been successful so far, and the City would like to continue to utilize CDBG funds for one more year to complete it.
- The Lakewood Village neighborhood does not meet the 51% Low/Moderate income threshold overall. Therefore, the City designated this overall CDBG-funded effort as an activity that qualifies under the national objective of Slums/Blight on an Area Basis, because it aids in the prevention or elimination of slums and blight in a defined geographic area.

### **Conclusions**

The CDBG funded landscaping (or other site improvement) of a private property in a Slum and Blight Area, may be eligible under 570.202(1) only if the landscaping comprises a secondary or lesser activity as part of a CDBG assisted rehabilitation of a residential structure on the property. And, such secondary site improvement activities may only be carried out when all conditions making the residential structure substandard have been eliminated, i.e., property is in compliance with local codes and Section 8 Housing Quality Standards. In Sunnyvale's case, the landscaping grants provided to individual property owners did not include any rehabilitation of residential structures.

If an eligible Community Based Development Organization (CBDO) operated in the area and the landscaping were a part of a neighborhood revitalization project per 570.204(a)(1), then the City may have used CDBG for landscaping privately owned property since a CBDO can undertake activities that are not otherwise eligible. However, this was not the case in the Lakewood Village Neighborhood enhancement effort.

In terms of the other CDBG-funded activities carried out in the Slum and Blight Area, such as sidewalk, street, utility repairs--these activities are eligible under 570.201(c)-Public Facilities and Improvements, since the improvements are publicly-owned. The City's repairs/improvement of sidewalks in the Lakewood Village neighborhood are eligible under this activity category.

#### **Required Corrective Actions and Resolution of Finding:**

After exhausting all other possible means of addressing this finding, the City was provided the following two options. We also requested that City staff determine the actual expenditures of CDBG funds used for private property landscaping activities for PYs 2003 and 2004, excluding funding for CDBG-eligible public improvements carried out in conjunction with the Lakewood Village Neighborhood Enhancement Project.

1. Return grant funds in the amount of total disallowed costs for Program Years 2003-04 and 2004-05 to its CDBG Line of Credit.
2. Offset the amount of CDBG funds used for ineligible activities, i.e., landscaping of private front yards, with the amount of local funds used to support CDBG-eligible public improvements, including program delivery costs and paid with non-CDBG City funds.

Detailed time allocation and expenditures documentation submitted by City staff prior to the issuance of this letter indicated that the amount of CDBG funds applied to disallowed costs was actually \$111,761.33. City staff also stated that the City intends to return this amount to its CDBG Line of Credit and to apply the funds toward various CDBG-eligible public improvement projects during the current 2005-06 Program Year.

Since this finding involves repayment of funds, it may only be closed-out after funds are actually received by the City's CDBG Line of Credit. However, it will still be necessary for the City to revise LVNEP project documentation and financial records. Also, revisions will have to be made within the IDIS System to reflect the project's reduced funding under Pys 2003 and 2004, and newly funded projects under the current program year. Additionally, the Annual Action Plans for Pys 2003, 2004 and 2005 must be amended accordingly and HUD notified when the amendments are completed.

### **Sub-recipient Administration**

The City continued the utilization of a two-year funding cycle for the CDBG funding process, specifically with respect to public services. Many cities in the Bay Area have adopted a similar funding policy, which has proven effective in streamlining the funding process, providing administrative relief to both local government staff and non-profit applicants and the opportunity for City and non-profit organizations to undertake longer-term strategic planning and maximization of funding resources. The Annual Action Plan approval process, including the public review process remains unchanged and second-year funding for public services sub-recipients is conditional and based on measured satisfactory performance during the first year of funding.

File documentation for all CDBG funded activities reviewed included comprehensive City/sub-grantee agreements, with the exception of the Neighborhood Enhancement project, which was directly implemented by the City. Program performance management goals, quantified objectives and timetables, approved budgets and funds requests, as well as quarterly reports which tracked the attainment of proposed actions and beneficiary data by quarter and cumulatively were available for public service projects. The 211-unit Homestead Park affordable housing project received CDBG rehabilitation assistance and exceeded the required minimum 51% low and moderate-income targeting and affordable rent thresholds.

Additionally, the City conducted an end-of-the-year on-site monitoring of each CDBG funded sub-recipient reviewed. Documentation included detailed correspondence describing the monitoring results, required and completed follow-up actions.

### **Timeliness of CDBG Funds Expenditures**

The CDBG Program regulations at 24 CFR 570.902 state that 60 days prior to the end of the grantee's current program year (i.e., April 30<sup>th</sup>), the amount of entitlement grant funds available to the recipient under grant agreements, but undisbursed by the U.S. Treasury, may not be more than 1.5 times the entitlement grant amount for its current program year. The City met the timeliness threshold for each of the program years reviewed.

### **Low and Moderate Income Benefit, Public Services & Administration/Planning Caps**

During the period covered by this review, the City exceeded the minimum 70% benefit to low and moderate (L/M) income persons threshold. CDBG funding for affordable housing projects also benefited 100% L/M persons. Public services and planning/program administrative percentages were below the maximum 15% and 20% statutory caps, respectively.

## HOME Program

### Commitment and Expenditure of Funds and Match

The City met its 24-month commitment of funds and commitment of CHDO set-aside funds deadline for all HOME allocations through FY 2003, as well as the five-year expenditure of funds deadline for all HOME allocations through FY2000. Over \$460,000 or 100% of HOME program income received to-date has been committed and expended toward eligible activities. Additionally, the average percentage of funds committed to CHDO projects per fiscal year allocation far exceeded the 15% minimum CHDO set-aside requirement and the overall rate achieved by the City covering all annual HOME allocations since 1992 was computed at 152%.

The majority of the City's 25% matching funds for expended HOME funds originated from local redevelopment 20% low-income housing set-aside funds. Match documentation was satisfactory and consistent with annual HOME reporting information. The City had accumulated excess match by the end of its 2004-05 Program Year.

### Policies and Procedures

#### **Concern 1: HOME Program policies and procedures are not consolidated.**

Many aspects of the funding and administration of HOME projects are similar to that required under the CDBG Program. In this respect, the City's established CDBG policies and procedures serve as the foundation for administering HOME such as in the areas of project application and review, funding allocation, compliance with Federal overlay requirements, construction oversight, on-going monitoring and financial and general record-keeping and reporting. However, the HOME Program has specific requirements that apply for example, to project underwriting/evaluation, execution of written agreements and on-going monitoring, which are distinct and more complex than the CDBG Program.

#### **Recommended Action:**

The City needs to develop comprehensive policies and procedures, i.e., operating manual, specifically for the HOME Program, which cover the funding application/ allocation process, project underwriting/evaluation criteria, scope of written agreements, project-specific and program-wide requirements, the City's grant administration and on-going monitoring responsibilities, the responsibilities of project owners, as well as requirements applicable to non-profit Community Housing Development Organizations (CHDOs). We would like to receive a copy of your policies and procedures operating manual for the HOME Program when completed.



### **Review of Project Files**

We reviewed two completed HOME-assisted projects developed by non-profit organizations, which also qualified as Community Housing Development Organizations. These included two rental projects, namely, Homestead Park which utilized \$1,100,000 in HOME funds in 2003 for rehabilitation and Stoney Pine Villa, which received \$780,000 in HOME funds in 1999 for new construction.

We determined that the City satisfactorily maintained all required project-specific documentation, including applications for funding, HOME loan and regulatory agreements, underwriting/subsidy layering, rents, affordability periods, tenant eligibility, occupancy thresholds, selection of HOME-assisted units and per unit allocation of costs, construction contracts and documentation of cost reasonableness, affirmative marketing plan and other project-specific Federal requirements.

At the intervals described under the HOME regulations, the City performed the required monitoring and on-site inspection of both projects selected for review. The City's monitoring consisted of selecting a sample number of HOME-assisted units, verifying actual rent and annual tenant income eligibility information provided by the owner and the inspection of individual units for compliance with local and Section 8 Housing Quality Standards. Progress in carrying out the affirmative marketing plan by the owner in order to fill vacancies in HOME-assisted units was also reviewed by the City.

### **Recommended Action:**

The City's HOME loan and regulatory agreements utilize local standardized formats and language and meet the basic HOME agreement requirements for the purposes of committing funds to an eligible activity, ensuring the applicability of affordability requirements and legal enforceability by the City. However, we suggest the incorporation of the following or similar language into future regulatory agreements, which conveys more explicitly that the HOME affordability requirements are to "run with the land" and not subject to revision by the PJ or any other entity.

*[...The affordability requirements shall apply without regard to the term or repayment of the Loan or the transfer of ownership and shall be imposed by deed restrictions or covenants running with the land, except that the affordability requirements may terminate upon foreclosure or transfer in lieu of foreclosure. The Affordability Restrictions shall be revived according to the original terms if, during the original affordability period, the Owner/Developer of record before the foreclosure, or deed in lieu of foreclosure, or any entity that includes the former Owner/Developer or those with whom the former Owner/Developer has or had family or business ties, obtains an ownership interest in the Project or property. ]*